Brexit – the future of the UK and EU indirect tax systems

Indirect Tax

20 December 2016

Lakshmi Narain reports on a key lecture at the indirect Tax Conference held in September where Paul Lasok QC provided an insightful analysis of the consequences of the referendum held on 23 June 2016

Put pithily, Paul noted that only three things can be said with certainty about the future for indirect taxes in the light of the impact of Brexit:

- the “future” for indirect taxes can be divided into two periods of time:
  - from now until the UK actually secedes from the EU; and
  - the period from the date of secession onwards.
- there is no obvious reason why Brexit would have any impact on the shape of the indirect taxes system in the EU; but there is likely to be a significant impact on certain UK indirect taxes.

- everything else is speculative because we have embarked upon the Brexit process without any plan and, it would appear, even without any idea at all about what is to emerge at the end of the process.

The future

Taking the first of the two periods – that from now to secession – there should be no change for the UK and EU indirect tax systems. The various Treaties shall cease to apply to the UK from the date of entry into force of a “withdrawal agreement” or, failing that, two years after notification in accordance with Article 50 unless that period is, as Article 50 provides, extended. It is worth noting that as, under Article 50(4), a withdrawing Member State “shall not participate in the discussions of the European Council or Council or in decisions concerning it” it is very likely that the withdrawing members influence can be anticipated to be inconsequential.

It is possible though that, even though EU law remains fully effective until the date of secession, the UK courts and tribunals will begin to move away from the strict application of EU law before then.

Royal prerogative

As regards the Government’s view that starting the process of seceding from the EU is a matter falling within the royal prerogative (the subject of current litigation), in reality, approval of the withdrawal agreement would have to be given by Parliament; secession can be effected only by repeal of the European Communities Act 1972 and this is a matter for Parliament. This is reflected in the proposal for the “Great Repeal Bill”. It has been stated that this legislation will be introduced in the next parliamentary session beginning with the Queen’s speech in May 2017.

The Government may need to make it clear to the EU when giving the notification required by Article 50 (planned for March 2017), that approval of any withdrawal agreement would have to be given by Parliament and, if that approval were not forthcoming, the Article 50 notification would be withdrawn.

From secession onwards

The second period, is much more uncertain. At this stage, it is wholly unclear what the relationship between the UK and the EU will be after withdrawal. Furthermore, the impact of the EU varies from one indirect tax to another.

Indirect taxes such as aggregates levy and air passenger duty (APD) are potentially affected only by the EU law principle of non-discrimination, the prohibition of restrictions on free movement of goods is relevant for aggregates levy and that for persons and services is relevant for APD and the prohibition of State aids is relevant to each of these taxes: otherwise the interaction with EU law is minimal.

For other taxes, like landfill tax, there is an indirect impact to the extent that the tax fits within EU environmental policy and the legislation creating the tax must (at present) be construed accordingly.

In relation to all such taxes, secession from the EU removes the potential for certain aspects of the tax to be challenged under EU law because EU law rights will cease to apply and the ability of the European Commission to raise (for example) a State aid challenge will disappear.

Paul noted that the more tricky taxes or imposts to deal with, in a Brexit scenario, are: customs duties, excise duties and VAT. For customs duties, Brexit offers a number of different permutations:

(a) exit from the EU customs union with the UK opting to become a free trade state;

(b) exit from the EU customs union with the UK operating its own customs law;

(c) exit from the EU customs union and a free trade deal with the EU; and

(d) the UK remaining within the EU customs union.

In relation to excise duties, secession from the EU could lead to the abandonment of the current system; but it could also be retained as a convenient form of international cooperation in the administration of excise duties or as a condition of any trade agreement between the UK and the EU.

For VAT, exit from the EU would permit the UK to abolish VAT altogether albeit the economic backdrop means that this is unlikely.

The most important change, however, would potentially concern the Halifax principle of abuse of right (or abuse of law) which is firmly anchored in a principle of EU law that EU law cannot be abused. In order to retain it, it would be necessary to legislate for it. Alternatively, the UK could abandon Halifax and replace it by a domestic general anti-avoidance rule – perhaps something like that introduced in Scotland and that proposed to be introduced in Wales (using concepts such as “artificial” and “genuine economic or commercial”; but, if the UK were operating within a VAT union with the rest of the EU, it seems that the UK would have to retain Halifax.

Conclusion

Paul concluded with a stark note of the pros and cons: from the perspective of the indirect tax system, Brexit is advantageous to the Government and disadvantageous for taxpayers. Quite simply, Brexit removes certain constraints on autonomous action from the operation of general principles of EU law down to the obligation to comply with the detail of the EU’s customs duty, excise duty and VAT regimes.